

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

In the Matters of)

Ameritech Corporation Telephone Operating)
Companies' Continuing Property Records)
Audit)

Bell Atlantic (North) Telephone Companies')
Continuing Property Records Audit)

Bell Atlantic (South) Telephone Companies')
Continuing Property Records Audit)

BellSouth Telecommunications Continuing)
Property Records Audit)

Pacific Bell and Nevada Bell Telephone)
Companies' Continuing Property Records)
Audit)

Southwestern Bell Telephone Company's)
Continuing Property Records Audit)

US West Telephone Companies' Continuing)
Property Records Audit)

CC Docket No. 99-117

ASD File No. 99-22

SUPPLEMENTAL REPLY COMMENTS OF
U S WEST COMMUNICATIONS, INC.

On October 22, 1999, the Federal Communications Commission
("Commission") released a Public Notice¹ indicating that the Accounting Services
Division ("ASD") had discovered "a substantial processing error" in its audit of
U S WEST Communications, Inc.'s ("U S WEST") continuing property records

¹ See Public Notice, Corrections to Audit Reports of the Bell Operating Companies' Continuing Property Records, CC Docket No. 99-117, ASD File No. 99-22, DA 99-2282, rel. Oct. 22, 1999 ("Notice" or "Public Notice").

("CPR") for hardwired central office equipment ("COE"). U S WEST indicated in its reply comments in the above-captioned proceeding that it would it would be amending its reply comments to reflect the revisions in the ASD's audit report.² After reviewing the ASD's revisions, U S WEST has determined that it is more appropriate to supplement its original reply (i.e., rather than amend it) because virtually nothing has changed in the ASD's audit report other than the ASD's estimate of the "projected cost of hardwired COE not found" -- which has increased by \$125 million.

The ASD's revisions do not address any of the statistical concerns/flaws that U S WEST and its expert, Ann Thornton of Deloitte & Touche, raised in previous comments and responses. In fact, the ASD's revisions exacerbate some of these concerns as Ms. Thornton notes in her attached letter:

[T]he reported "correction" that the FCC has made does nothing to mitigate the criticisms and concerns that have been raised in our prior letters. In fact, the latest revisions raise even more questions about the thoroughness of the auditors, the appropriateness and completeness of their procedures, and the validity of their estimates.³

I. NEITHER THE PUBLIC NOTICE NOR THE ASD'S REVISIONS TO THE U S WEST AUDIT REPORT PROVIDE AN ADEQUATE EXPLANATION FOR A "CORRECTION" OF \$125 MILLION

In previous filings on the CPR audit, U S WEST has criticized the ASD for failing to document its statistical methods. Nothing has changed with respect to

² U S WEST Reply Comments at 2. Due to the lateness in receiving the ASD's audit report revisions, neither U S WEST nor its experts had sufficient time to review and evaluate the ASD's changes prior to the October 25, 1999 due date for filing reply comments. As a result, U S WEST filed its reply comments without reference to the ASD's revisions.

the ASD's \$125 million "correction." Neither the Public Notice nor the ASD's revised audit report provide an inkling of what actually happened or why it took the ASD over a year to discover its error. Clearly, the statement that "a portion of the audit data was inadvertently left out of the statistical calculations"⁴ is insufficient to explain a \$125 million "correction." In fact, this statement raises more questions than it answers given that: 1) the number of CPR errors reported did not change; 2) the estimate of the percentage error decreased; and 3) the estimate of the dollars of error increased significantly.⁵ As Ms. Thornton states:

The explanation of the FCC, that "a portion of the audit data was inadvertently left out", provides no indication of why the estimated percentage error rate decreased while the point estimate of dollar error increased. Typically, one would not expect to see these values moving in opposite directions.⁶

If anything, the ASD's undocumented "correction" casts even more doubt on the validity of the ASD's statistical procedures -- which U S WEST believes were "fatally flawed" prior to the correction.

II. THE DELAY IN REPORTING AN ERROR OF THIS MAGNITUDE CLEARLY CALLS INTO QUESTION ANY QUALITY ASSURANCE PROCEDURES THAT THE ASD MAY HAVE EMPLOYED IN ITS AUDIT

Audit findings are not "one time" rough estimates. Auditors have a duty to employ quality assurance procedures so that any material errors are detected prior to finalizing audit reports. "It is typical to have an independent recalculation

³ Thornton Attachment at 2.

⁴ Notice at 1.

⁵ Thornton Attachment at 2.

⁶ Id.

performed of any statistical estimate that projects significant monetary error.”⁷ If the ASD’s “correction” is any indication, it appears that the ASD’s quality assurance procedures were woefully inadequate. As Ms. Thornton states:

It is customary to perform thorough, detailed quality assurance procedures around statistical estimates that appear in audit reports, especially when these estimates may be used to support recommended adjustments to financial statements. Appropriate quality assurance procedures should detect significant errors and prevent them from being included in an audit report.⁸

III. THE PUBLIC NOTICE’S INFERENCE THAT U S WEST COULD HAVE AND SHOULD HAVE FOUND THE ASD’S ERROR IS BASELESS AND IN NO WAY LESSENS THE SERIOUSNESS OF THE ASD’S ERROR

The Notice infers that U S WEST could have and should have “caught” the ASD’s error.⁹ There is no basis for this inference.¹⁰ As Ms. Thornton states in her attached letter, U S WEST did not have sufficient data to recalculate the ASD’s estimate and, even if it did, U S WEST would have been ill-advised to do so:

It would have been inappropriate for US West to try to recalculate the statistical estimates. In our August 1998 and January 1999 letters, we advised US West that the FCC’s estimates were possibly invalid and that the large precision associated with the estimates gave reason to doubt the acceptability of using the estimates. It makes sense that US West would not have tried to recalculate estimates that could be seriously flawed.¹¹

⁷ Id.

⁸ Id.

⁹ Notice n.3.

¹⁰ Ms. Thornton also takes issue with the Public Notice’s inference. “While the FCC implies that US West should have and could have recalculated the statistical estimates, we believe that US West should not have and could not have recalculated the estimates.” Thornton Attachment at 3.

¹¹ Id.

As such, the Commission should reject any arguments which attempt to assign blame to U S WEST for not finding the ASD's error, particularly when U S WEST has challenged the validity of the ASD's estimates since the CPR audit report first became available.

IV. EVEN IF THE ASD'S REVISED ESTIMATE IS VALID THE SIZE OF THE PRECISION RANGE RENDERS IT MEANINGLESS FOR DECISIONMAKING PURPOSES

In its prior comments, U S WEST expressed concern over the size of the precision range around the ASD's estimate of missing plant and noted that an estimate with such a large precision range was of little or no value for predictive purposes.¹² The ASD's revised estimate does nothing to alleviate this concern -- in fact, it is exacerbated by the ASD's "correction." The ASD's revisions increase the precision from +/- \$197.4 million to +/- \$242.4 million at a 95% confidence interval¹³ -- an increase of over 20%. With the ASD's "correction," the total range of uncertainty has increased to \$484.8 million, as compared to \$394.8 million.¹⁴ This is particularly relevant given the fact that "no one point in the confidence interval is statistically preferable to any other point."¹⁵ Thus, even if the ASD's estimate is valid, it is virtually meaningless for predictive purposes as Ms. Thornton notes:

We reiterate that, even if the estimate is in fact valid, the size of the precision range, because it is so large in relation to the estimate, creates doubt as to the practicality of using the range for concluding as to the actual amount of error in the population.

¹² U S WEST Reply Comments at 18.

¹³ Thornton Attachment at 4.

¹⁴ Id.

¹⁵ Id.

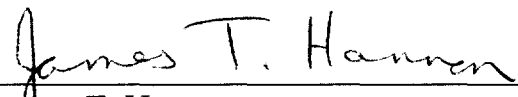
Therefore, the Commission should reject the ASD's estimate -- even if, by chance, it finds no other fault -- because the ASD's estimate still is of no use for predicting the amount of missing COE plant.

V. CONCLUSION

As U S WEST has demonstrated in the foregoing supplemental reply comments and in previous comments, the ASD's estimate of missing hardwired COE investment is fatally flawed. The ASD's revisions do nothing other than highlight the deficiencies of its quality assurance measures and the fact that the precision range is so large as to render any estimates of no value for predictive purposes.

Respectfully submitted,

U S WEST COMMUNICATIONS, INC.

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November 3, 1999

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November 1, 1999

Mr. Mark Link
Executive Director – Corporate Accounting
US WEST Communications, Inc.
1801 California Street
Denver, CO 80202

Dear Mr. Link:

Deloitte & Touche LLP was asked by US West, Inc. to read and provide comments related to sampling methodologies and issues as described in several documents:

- the draft FCC report, “Audit of Continuing Property Records of US West as of June 30, 1997; Report of Audit Findings” (the “August FCC Report”)
- the December 22, 1998 draft of the “Audit of Continuing Property Records of US West as of June 30, 1997; Report of Audit Findings” (the “December FCC Report”).
- Affidavit of Robert M. Bell, PhD, filed September 23, 1999
- Affidavit of James K. Loebbecke, CPA, filed September 23, 1999
- Comments of AT&T Corp, filed September 23, 1999
- MCI Worldcom Comments, filed September 23, 1999
- Letter of William Kennard to Congressmen Tanzin and Dingell dated February 24, 1999

We provided US West with a letter dated August, 18, 1998 containing our comments on the “August FCC Report”, a letter dated January 8, 1999 containing our comments on the “December FCC Report”, and a letter dated October 25, 1999 containing our comments on the remaining documents listed. A copy of those letters is attached hereto.

You have now asked us to read a revised draft of the FCC report, released on October 22, 1999 pursuant to Public Notice DA 99-2282 (the “October 1999 FCC Report”). This report was released after errors were found in the statistical calculations reported in prior audit reports (the “August FCC Report” and the “December FCC Report”, the first of which was originally released more than a year before the recently reported “correction”).

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The description of the audit and the statistical methodologies applied appears to be very similar to that in the original audit report. Therefore, the reported "correction" that the FCC has made does nothing to mitigate the criticisms and concerns that have been raised in our prior letters. In fact, the latest revisions raise even more questions about the thoroughness of the auditors, the appropriateness and completeness of their procedures, and the validity of their estimates. The following aspects of the revised audit report are notable:

1) The FCC failed to document in sufficient detail the nature of the mistake that was made.

The FCC states: "Regarding the US West report, a portion of the audit data was inadvertently left out of the statistical calculations." In the past, we have criticized the FCC for inadequately documenting its statistical methods. As in the past, the FCC has reported a result (i.e., a reported "correction" of more than \$125 million) without providing information about how the result was derived.

2) Even though the number of CPR errors reported did not change, the estimate of the percentage error rate decreased while the estimate of the dollars of error increased significantly.

In the revised report, as in the original report, the FCC reported that 894 of 1,188 CPR line items in the sample were correct (see Appendix B, p. 14 in both reports). If this is true, then it is unclear why the estimated error rate in the population decreased from 26.11% to 25.35% while the point estimate of dollars of error in the population increased from \$378.6 million to \$505.8 million and the precision at a 95% confidence level increased from +/- \$197.4 million to +/- \$242.4 million. The explanation of the FCC, that "a portion of the audit data was inadvertently left out", provides no indication of why the estimated percentage error rate decreased while the point estimate of dollar error increased. Typically, one would not expect to see these values moving in opposite directions.

3) The size of and delay in reporting the "correction" casts doubts on the adequacy of the quality assurance process associated with the FCC audit reports.

It is customary to perform thorough, detailed quality assurance procedures around statistical estimates that appear in audit reports, especially when these estimates may be used to support recommended adjustments to financial statements. Appropriate quality assurance procedures should detect significant errors and prevent them from being included in an audit report. For example, it is typical to have an independent recalculation performed of any statistical estimate that projects significant monetary error.

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4) Bayesian analysis has still not been removed from the report.

In prior letters, we have argued that the Bayesian analysis was not adequately documented and therefore provided little support for the FCC's classical statistical estimates. Once again, the FCC has included Bayesian analysis to "corroborate our statistical findings" (October 1999 FCC Report, Appendix B, p. 14). It is unclear that this reported "corroboration" has any value, given that the Bayesian analysis was also used to corroborate the FCC's prior findings, when the FCC's point estimates were more than \$125 million lower.

5) The FCC implies that US West should have and could have recalculated the statistical calculations in the report. We disagree.

The FCC states: "Before the final audit reports were released, each company was provided with a copy of the draft audit report and sample observation data necessary to confirm the statistical calculations and inferences in the report. We note that the carriers did not address the errors that were found in ASD's reexamination" (Public Notice DA 99-2282). While the FCC implies that US West should have and could have recalculated the statistical estimates, we believe that US West should not have and could not have recalculated the estimates.

It would have been inappropriate for US West to try to recalculate the statistical estimates. In our August 1998 and January 1999 letters, we advised US West that the FCC's estimates were possibly invalid and that the large precision associated with the estimates gave reason to doubt the acceptability of using the estimates. It makes sense that US West would not have tried to recalculate estimates that could be seriously flawed.

Even if US West had tried to recalculate the statistical estimates, the FCC probably did not provide US West with enough information to do so. Based on our understanding, the FCC provided US West only with the audit report and the sample of 1,188 items (these are the only two items that the FCC mentioned in Public Notice DA 99-2282, cited above). US West would have also needed a listing of the 1,131 offices used for sampling to be able to recalculate FCC's statistical estimates (including recalculations of formulas 8-9, 11-15, and 17-22 from the October 1999 FCC Report). Information on which 1,131 offices were used in the extrapolations is unavailable because, as noted in our prior letters, the FCC did not clearly describe and demonstrate how the sampling population was defined.

Thus, if the FCC had provided US West with additional data, it might have been possible for US West to reperform the statistical calculations performed by the FCC. These calculations could be used to check arithmetical accuracy but would not be expected to provide reliable statistical estimates. In fact, we have raised serious questions about the reliability of the

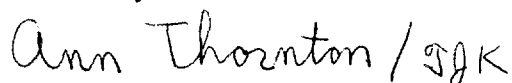
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FCC's statistical methodologies (for example, see Observations 1-12 in our October 25, 1999 letter). The October 1999 FCC Report does not eliminate any of these concerns; indeed, some problems we had with the original extrapolation are now exacerbated.

For example, we had expressed concern in prior letters that the precision range around the FCC's dollar estimate might be too large to be useful. Based on the new reported "corrections" now included in the October 1999 FCC Report, the precision has increased from +/- \$197.4 million to +/- \$242.4 million at 95% confidence. Therefore, the total range of uncertainty around the estimate is now \$484.8 million (i.e., $2 \times \$242.4$ million), as compared to the prior range of \$394.8 million. (As we have stated before, the size of the precision range is significant, because based on the statistical literature, no one point in the confidence interval is statistically preferable to any other point.)

In summary, the revised October 1999 audit report does nothing to respond to observations made in our letters of August 18, 1998, January 8, 1999, and October 25, 1999. In fact, the revised report raises some additional concerns, as noted above. In addition, we continue to have concerns that the approach taken by the ASD may result in invalid sampling estimates. We reiterate that, even if the estimate is in fact valid, the size of the precision range, because it is so large in relation to the estimate, creates doubt as to the practicality of using the range for concluding as to the actual amount of error in the population.

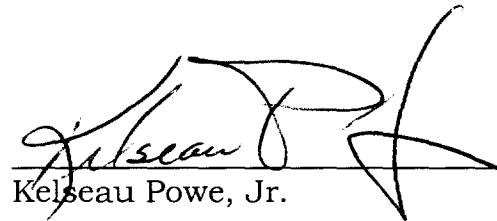
Yours truly,

Handwritten signature of Ann Thornton, followed by the initials JGK.

Ann Thornton, Director
National Director – Data Quality and Integrity Services

CERTIFICATE OF SERVICE

I, Kelseau Powe, Jr., do hereby certify that on this 3rd day of November, 1999, I have caused a copy of the foregoing **SUPPLEMENTAL REPLY**
COMMENTS OF U S WEST COMMUNICATIONS, INC. to be served, via first class United States Mail, postage prepaid, upon the persons listed on the attached service list.


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